CERTAIN PRINCIPLES OF VALUATION IN RATE CASES

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As the valuation problem develops it becomes increasingly clear that the term "value" may be properly used in several different senses, and that what is value for one purpose is not necessarily value for another. The best results are undoubtedly obtained when the problem of valuation is worked out solely with reference to what is just and reasonable with regard to the specific purpose for which the valuation is to be used. Certain facts and certain elements of value will doubtless be considered in arriving at a judgment as to value for tax or rate or purchase purposes. This is particularly true of the important fact of cost of physical property, both actual cost and reproduction cost. But the degree of consideration given to certain facts may vary greatly with the purpose of the valuation, and certain facts and elements may be considered for one purpose and entirely excluded for another. This principle seems to be fully recognized in almost all of the recent court and commission decisions in relation to fair value for rate purposes.

Standard of Value

It has frequently been stated that there can be no rule or formula for the determination of fair value for rate purposes. Each case must be considered on its own merits, and such result or value arrived at as may be "just and right in each case." "It is not a matter of formulas, but there must be a reasonable judgment having its basis in a proper consideration of all relevant facts."[1] The supreme court has gone no further than to state that it is present, as distinct from past, fair value that is to be determined, and to mention certain of the elements to be considered in such determination. The court, however, has given no indication as to how these various elements should be combined to produce the final result. It does not indicate the

[1] The Minnesota Rate Cases, 230 U. S. 353, 434, June 9, 1913.

relative weight to be attached to the various elements nor does it indicate that in a particular case any weight need attach to certain elements. In view of the complexity of the problem it is probably fortunate that the courts have not as yet attempted a more illuminating definition of fair value. It is recognized that the entire problem is in a developmental stage and that there is danger of creating precedents that may compromise future action when the entire problem has been more fully disclosed.

In considering fair value for rate purposes it is important to bear constantly in mind that the determination of fair value is a part of the process of determining a reasonable rate of charge. By reasonable rate as here used we mean the reasonableness of the rate schedule as a whole and not the adjustment of the various specific rates that go to make up the complete rate schedule. A reasonable rate of charge in the sense of a reasonable rate schedule is a rate that gives the company reasonable compensation for the entire service which it renders the public. In the case of an appropriate and normally successful public utility enterprise, reasonable compensation is equivalent to the normal cost of production. Normal cost of production includes normal operating expenses plus a normal rate of return on a normal capital cost. The aim of public regulation is to accomplish what in other industries is assumed to be accomplished automatically by free competition, that is, to limit the price charged to the normal cost of production. There is no reason why in the case of a virtual monopoly the public should be required to pay more than the normal cost of production, and sound reason why in the long run the public cannot pay less. Normal cost of production is the amount which in the long run it is necessary to pay to secure the utilities demanded by the public. It is the amount that will secure an equilibrium between demand and supply.

In the case of a commodity requiring a large fixed investment the determination of a normal cost of production is a complex process, in the working out of which there is room for a wide divergence of opinion. To the normal cost of labor and materials there must be added a fair estimate for depreciation and a fair return on capital cost. The determination of a normal return upon a normal capital cost requires the determination of two very difficult and complex problems: (1) What is the amount of the normal capital cost, and, (2) what constitutes a normal return on such amount. Normal capi-

tal cost as applied to a new enterprise is a comparatively simple concept. But what is it as applied to a long-established enterprise—to a water supply plant, a gas plant or a railroad system? Is it normal cost at the time originally installed or last renewed, or, on the other hand, is it the present cost of reproduction? Is it actual cost or reproduction cost?

Appraisals of physical property considered in rate cases have largely been estimates of reproduction cost. The reproduction theory in its strict form involves the reproduction of the service rather than the reproduction of the identical plant. If the old plant were wiped out what would it cost at present to construct and operate a plant capable of performing the service now performed by the old plant? As thus stated, the reproduction method has so many difficulties that it is practically never employed. In most cases it is exceedingly difficult and expensive to determine the design of an equally efficient substitute plant. In the case of a railroad, for example, the cost of determining a substitute location and of estimating the operating cost thereon would be so great as to render it entirely impracticable as a factor in rate regulation. The cost of reproduction in practice, therefore, instead of meaning the cost of a substitute plant of the most modern approved design, capable of performing the same service as the existing plant, has come to mean the cost of a substantially identical reproduction of the existing plant. By a further modification of the cost of reproduction method which is coming more and more into use, the cost of reproduction is made to mean not the cost at present prices of land, labor and materials, of reproducing a substantially identical plant under *present conditions*, but the cost at present prices of land, labor and materials of reproducing a substantially identical plant under the *actual conditions* under which the existing plant was originally constructed. Under this method expenditures actually incurred in the development of the present property are fully allowed for, even though they would not be met with in a reproduction of an identical substitute plant. On the other hand, certain expenditures that have not been incurred in the development of the existing property but would be incurred in the reproduction of the existing property, are excluded. The reproduction method has been modified by the practical difficulties in the way of its strict application, and by the recognized equities created by actual cost and actual investment.

In failing to give even more consideration to actual cost in determining fair value, commissions and courts have often stated that the actual cost was impossible of determination. This it seems has been largely the result of a somewhat confused conception of actual cost. Actual cost properly considered may in a great majority of cases be determined with at least as great accuracy as reproduction cost. The confusion has arisen from identification of actual cost with book cost or first cost of original units, or both. Properly speaking, actual cost is the first cost of the identical units now in use and not the first cost of the original units. A first essential to the determination of either actual cost or reproduction cost is a complete inventory of property units in use. A second essential in both cases is the determination of the approximate time at which each such unit was installed. Records are usually available showing for any period the prevailing prices of labor and materials entering into construction costs. From such records, supplemented in many cases by fragmentary data obtainable from the books of the company, it is possible to apply unit costs. It is believed that such estimates will in most cases come nearer to the true actual cost than will present estimates of reproduction cost come to the true reproduction cost.

The St. Louis Public Service Commission has practically adopted actual cost as its standard as applied to structures and equipment, but in the case of land has used present market value. The New Hampshire Public Service Commission seems inclined to use actual cost as the normal controlling standard. The Nebraska commission, while adopting reproduction cost as the only practical method of obtaining a starting point, has recognized actual investment as the standard which should govern the future relations of the utility company and the public. The decisions of the California, Wisconsin and New York commissions show that they are inclined to give great weight to actual cost when such cost has been established.

The determination of a standard of value applicable to existing utilities will be worked out, if at all, by the slow and piecemeal process of court decision in numerous cases. The final answer can be given only by the supreme court of the United States. It would seem, however, that, as to the future, legislative bodies and commissions might at once adopt a standard. If normal actual capital cost were adopted as the rule for the future with reference to appropriately

located and successful enterprises, rate regulation and accounting methods would be much simplified and the relations between the utilities and the public placed on a much more equitable and dependable basis.

Land

In spite of the evident desire of a number of the commissions to give great weight to actual investment in determining fair value, an exception has apparently been made in the case of land. Here the decisions of the supreme court, stating that it is present value that is to be ascertained, have seemed to require that land should be taken either at its present market value or its reproduction cost.

In its decision in the Minnesota rate cases[2] the United States supreme court says that while "it is clear that in ascertaining the present value we are not limited to the consideration of the amount of the actual investment," yet there is no just ground for placing a value on railway lands in excess of the actual investment and in excess of the value of similar property owned by others merely on account of a conjectural cost of acquisition and consequential damages, and on account of percentages or other overhead expenses. The court concluded that "The company would certainly have no ground for complaint if it were allowed a value for these lands equal to the fair average market value of other land in the vicinity without additions by the use of multipliers or otherwise to cover hypothetical outlays."

In the case under consideration, the increment in the land value had been much more than adequate to cover all costs of acquisition and consequential damages, including any overhead expenses incurred for engineering, superintendence, legal expenses or for interest or taxes during construction. If the case had been that of a new road where there had been no increment in land value to offset these expenses connected with the acquisition of the land, it does not seem probable that the court would have refused to consider them in fixing the fair value for rate purposes. It seems that through the application of the principle laid down by the court in the Minnesota rate cases all of the advantage due to increment in land value does not inure to the benefit of the public service company, but that such increment is first used to offset or amortize all capital expenditures incurred in the acquisi-

[2] *Ibid.* 353.

tion of the land and the carrying charges on such outlay during the period of construction.

It seems, therefore, that in the case of railway land the court will measure the allowance chiefly by the market value of neighboring lands, but that it will also give some consideration at least to the actual cost to the railroad of acquiring its lands in case such cost is greater than the present market value of the land for other than railroad uses. The court specifically rejects the cost of reproduction method of estimating the value of railway land. In this it apparently makes a distinction between land and other physical property. Possibly such distinction is made on the theory that railway land differs from other railway structures in that it has a definite value for other uses. It is clear that railway structures other than land would have merely a scrap value for other than railway uses. The difference here, however, is merely one of degree, and its importance is greatly overestimated. Railway land can not be disposed of for other uses without scrapping the entire property. If a railroad right of way were sold for farm purposes, the loss due to the scrapping of the roadbed would more than offset any increment in the selling price of the land.

As we have already noted, fair value for rate purposes in the case of a virtual monopoly can not properly be based on exchange or market value. Value when used to denote the amount on which such a company shall be allowed to earn a fair return is normally based on cost, either actual cost or reproduction cost. It seems illogical to introduce any question of market or exchange value unless such market or exchange value has a direct bearing on either actual cost or reproduction cost.

Actual cost seems particularly appropriate as a standard of value in the case of land used by a public utility. Rates of charge should not be affected by real estate activity or reactions. The public utility is not formed to speculate in land. Though some compromise may be desirable as to the past, actual cost should be adopted as the normal standard for the future. But if this is not done it will be logical and just that appreciation in land value be treated as income or considered in fixing the rate of return. There can be no doubt that appreciation *upon which a return is earned* does constitute a profit of a very real sort. If a company claims a return on appreciated value it cannot equitably hold that such appreciation does not constitute a part of its income. Increments and profits of every kind

enjoyed by a company must necessarily be considered a part of the total compensation that the company receives from the public. In so far as there are increments and profits arising from increase in land values it is clear that such increments and profits should in a rate proceeding be considered either as income or as an offset in fixing the rate of return.

Pavement over Mains

Courts and commissions almost without exception have in numerous cases refused to include in fair value for rate purposes the cost of reproducing pavement laid over mains without expense to the company. Under the strict reproduction method such pavement would be included, as the existing plant and mains could not be reproduced without cutting through and reproducing the pavement. In refusing to include pavement laid without expense to the companies the commissions are in effect applying the modified reproduction method, that is, using the cost of reproduction at present prices of labor and materials but under the physical conditions under which the existing property was actually constructed.

In the Consolidated Gas case, Justice Peckham in delivering the opinion of the court made a general statement in regard to including property at its present appreciated value, which, while doubtless intended chiefly to apply to land valuation, might also be construed to include the valuation of mains and services, and thus to decide that the present replacement value of the mains should be considered regardless of the question of pavement laid by the city. The courts and commissions have not in general construed Justice Peckham's opinion in this way, and the more recent opinion of the court in the Minnesota rate cases rejecting the reproduction method as applied to land seems to confirm the belief that when the question of pavement over mains comes squarely before the supreme court the reproduction method in its strict form will also be rejected as applied to this item of property.

Accrued Depreciation

The United States supreme court in two cases has held that there must be a deduction from cost new to cover accrued depreciation in determining fair value for rate purposes.[3] Following this ruling

[3] Knoxville *vs.* Water Company, 212 U. S. 1, Jan. 4, 1909. Minnesota Rate Cases, 230 U. S. 352, June 9, 1913.

of the highest court the commissions have almost unanimously based fair value on cost-less-depreciation. The principal exception is that of the St. Louis Public Service Commission. In its report on the Southwestern Telegraph and Telephone Company, October 14, 1913, the St. Louis commission says, "Where there has been no regulation in the past and where it can be shown that there was no necessity of establishing a depreciation fund equal to the consumption of estimated life of each item of equipment, deduction for theoretical depreciation in a rate case involving a large 'piecemeal' built property in a normal and efficient state becomes in fact merely a confiscation of past profits."

Depreciation is a problem in cost accounting. It is concerned with the allocation to each year's operating accounts of the waste in the instruments of production attributable to the year's operations. The cost of materials purchased and entirely consumed in the course of the year's operations is invariably included in ordinary operating expenses. The capital required to purchase and carry such materials during the turn-over period is a part of the working capital. But some materials or instruments of production are not used up during the first year but have a life of 3, 10, 20, 50 and 100 years. They are consumed in operation just as surely as the former and constitute just as real a part of the cost of production. Their cost (exclusive of scrap value) must, however, be distributed over the full life period. The capital required to purchase and carry these long-lived consumable materials may also be considered a part of the working capital. It is this element of interest on capital that so greatly complicates the depreciation problem.

Depreciation is concerned with the maintenance of the integrity of the investment in depreciable property at a uniform annual cost. Such costs cannot be determined without some reference to interest on reserves and investment. The entire problem, therefore, may be simplified by considering depreciation as the adjustment necessary to secure a uniform investment cost. The supply of a public service must be considered a continuous process. Management or ownership may change but the plant and the service and the depreciation process are assumed to go on forever. The annual investment cost includes not only interest but also the repairs, renewals and replacements necessary to keep the property permanently in good working condition. The rights of the consumers using the supply at different periods de-

mand that the annual charges attributed directly to the investment shall be as uniform as possible.

As a problem in cost accounting the accrued depreciation and the annual allowance for depreciation are interdependent. Our theory in regard to an annual allowance for depreciation will necessarily control that in relation to the amount of accrued depreciation and vice versa.

It needs no extended argument to demonstrate that, if the moneys paid into the depreciation reserve are assumed to accumulate at compound interest for the sole benefit of the depreciation reserve, they do not constitute a return to the owner of any part of his original investment. Unless, therefore, he is allowed to earn a return on cost-new, a part of his actual investment is confiscated. There are, however, serious objections to the sinking-fund method of allowing for depreciation. It is assumed that a fund is set aside and made to accumulate at a prescribed rate of interest. Presumably it is to be invested in outside securities and kept as an entirely distinct fund. The assumption of a separate fund greatly complicates the accounts. It is usually merely an assumption both as to its existence and as to the rate at which it accumulates. Business practice recognizes that ordinarily the most natural, the most secure and the most profitable use that can be made of a depreciation reserve is to retain it in the business to meet the additional capital requirements for plant and working capital. Fundamentally the depreciation reserve is a part of the entire capital needed to carry on the enterprise. There is no reason why a part of the total capital should be set apart and assumed to accumulate at a rate different from that earned on the entire investment. The entire enterprise is a unit and the profits, whatever they may be, are the earnings of the entire investment. One part of the investment should not be assumed to earn at an arbitrary rate and the rest at a different rate.

The depreciation reserve is built up during the early years of the enterprise. It is during such earlier years that the payments into the depreciation reserve are normally greater than the annual expenditures for renewal. When a utility has settled down to a constant average of wear and age, the annual allowance for depreciation is, under the straight-line method, about equal to the annual expenditures for renewal, and, under the sinking-fund method, much less than such annual expenditures. As almost every utility is built

somewhat on the piecemeal plan and as it particularly is true that there are normally a considerable number of additions to capital during the first twenty years of an enterprise, there would seem to be abundant opportunity for the investment of the entire depreciation reserve in such additions. It is also to be noted that a large part of this reserve may be invested *permanently* in the business. When a utility has settled down to a constant average of wear and age, the depreciation reserve remains at a constant percentage of cost-new. It is particularly appropriate, therefore, that this permanent reserve should be permanently invested in the business. And if this is done why should it be assumed to be earning for a depreciation fund at the rate of 4 per cent while the business as a whole is earning 6 per cent?

The uniform investment-charge method takes account of the fact that ordinarily the safest and best use that can be made of a depreciation reserve is to invest it in the business; that the reserve, therefore, becomes an integral part of the entire business and cannot be assumed to earn at a different rate from that of the business as a whole; that the expenditures for renewals in the earlier years are much less than later when the *average* age of the various units constituting the plant is at a maximum; that the depreciation reserve is for the most part accumulated from the excess of the depreciation allowance over the actual renewals during the earlier years; that investment of the reserve in the business decreases the amount of capital to be furnished by the owners and correspondingly decreases the percentage return *as based on cost-new.*

With a declining percentage return as based on cost-new the only way to secure a uniform combined annual charge for interest and depreciation is so to adjust the depreciation allowance that the increase in percentage charge for depreciation based on cost-new will exactly offset the decline in the percentage return.

In order to determine the percentage on cost-new that will provide a uniform annual charge for return plus depreciation, add to the fair rate of return the per cent on cost-new, that, set aside annually and compounded at the same rate of interest as the fair rate of return, will, within the equated life of the depreciable property, exactly equal the cost-new of such depreciable property. Conversely, to find the accrued depreciation in an existing plant under the uniform-annual-investment-charge method, find the amount that should

be in the depreciation reserve, assuming that the annual depreciation allowance had been set aside from the initiation of the enterprise in accordance with the method above described.

Assuming the adoption of the uniform-annual-investment-charge method, the straight-line method or the sinking-fund method as the proper method for the treatment of depreciation as regards a new enterprise or as regards the future of an existing enterprise, is it necessary to qualify such method as regards assumptions as to the past of a company that has heretofore not been subject to regulation? Can we assume that the theory that we apply to the future has been in operation since the initiation of the enterprise? If we determine that the sinking-fund method is upon the whole most just and practicable, can we assume that a fund has been accumulating on this basis and is now earning interest and that the amount of such interest may be deducted from the annual allowance that would otherwise be required to meet current renewals? Or if we adopt the uniform-annual-investment-charge method, can we assume that the depreciation reserve is equal to the amount that it should have reached had this method been applied from the initiation of the enterprise and that, therefore, it is just to deduct this amount from cost-new to determine fair value for rate purposes? It seems that both these questions must be answered in the affirmative. There is no question that depreciation is an operating expense. There is no question but that it is an expense that must by some method be apportioned over the entire life of the depreciable property. There is no way that this can be done except by apportioning a fair share of the burden to the operating expenses of each year since the initiation of the enterprise. To be sure there may be cases where the past profits of an enterprise have been insufficient to pay a fair rate of return and at the same time set aside a proper depreciation reserve. The situation may demand that, in prescribing regulations for the future, the company be allowed to reimburse out of the earnings the amounts by which past earnings have failed to provide an amount adequate to pay operating expenses including depreciation and a fair return on the investment. It is important to note that this shortage is properly treated as a deficit to be reimbursed and not as additional outlay to be capitalized.

Going Value

We may take it as an established principle that the determination of fair value for rate purposes is normally one step in the process of determining what is a fair cost of production. Fair value is therefore normally based on cost, either actual cost or replacement cost. When, therefore, we speak of going value as an element of fair value for rate purposes it must be assumed that such value will be based on a necessary cost actually entering into the cost of production. It cannot logically be based on any monopoly or good will element, or any estimate of the value in money to the company of its developed earning power. As a reasonable rate of return is normally based on cost of production, either assuming the actual investment or assuming a present reproduction of the property, it would seem that going value must either be based on the actual cost of establishing the business or on the estimated cost of reproducing the business. This in general has been the attitude of courts and commissions in so far as they have considered going value in the determination of reasonable rates.

Courts and commissions have in most cases in recent years considered going value as the actual cost of establishing the business. The rule laid down in many cases by the Wisconsin Railroad Commission, and followed by various other authorities, is to consider as going value the uncompensated losses incurred in the development of the business. That is, going value is ordinarily the amount by which early failure to earn a fair return has not been offset by subsequent earnings in excess of a fair return. A few authorities, notably the two New York commissions, have approved in general this method of determining the cost of establishing the business, but have maintained that, inasmuch as it is only the net or uncompensated loss that is considered, it is scarcely appropriate to include such cost in fair value. It is more appropriately allowed for in the rate of return. If returns are impaired while the business is being established it seems appropriate that the impairment should be reimbursed by more liberal returns in profitable years. Under the theory adopted by the Wisconsin commission the cost of establishing the business is not a permanent sum, but varies from year to year as it is increased by failure to earn a fair return or reduced by returns in excess of a fair amount. It is treated not as a part of the capital

cost but as an amount to be reimbursed out of future earnings. It seems inconsistent, therefore, to consider such cost a part of fair value. It is appropriate to allow for it in fixing the rate of return.

In some exceptional cases public utility enterprises may find it necessary under conservative management to capitalize business development costs. Ordinarily, however, this is unnecessary and would be considered poor business management. The better way is to forego dividends until earnings are adequate to cover ordinary operating expenses, cost of securing new business and interest on bonds. As this is the rule approved by the best practice it seems appropriate to assume its existence in determining cost of production as the basis for a reasonable rate of charge. Ordinarily, therefore, cost of establishing the business will not be included in capital cost but will be reimbursed out of earnings.

In opposition to the method of reimbursing out of earnings the cost of establishing the business, it is argued that such cost is as much a part of the capital cost as is the cost of the physical property. This being so it is a cost that should be paid for by all users throughout the life of the utility and not by the users of the earlier years. By reimbursing this cost out of earnings the consumers during the period of such reimbursement are taxed for something that will be of as much benefit to the future consumers as to themselves. This argument is not convincing. The public as users of public utilities are as much interested in the future as in the present. Public policy with relation to public utility rates cannot be limited by an estimate of cost to a particular consumer at a particular moment. Public policy will look to the future as well as to the present, and adopt the rate policy that offers the largest measure of public advantage, even though the chief advantage be secured by future consumers rather than by those of the present. The rate paying public can well afford to bear the temporary extra cost of amortizing all intangible and questionable elements of capital cost. This will tend to safeguard the actual investment of the security holders and to reduce the cost of production and the rate of charge.

The New Jersey commission has included in going value not only the early deficits but also the cost of getting new business, including the cost of new business obtained in recent years and charged to operating expenses. In the case in question the commission had

to do with a heretofore unregulated utility. The inference is that, if a utility while subject to regulation charges the cost of obtaining new business to operating expenses, it will not be allowed to include such costs in the fair value of its property in any subsequent rate regulation proceeding.

Most commissions in considering the cost of establishing the business have considered the estimated actual cost and not the estimated reproduction cost of such establishment. Even where commissions have relied upon the reproduction method in determining the cost of the physical property, they have usually tried to estimate the actual rather than the reproduction cost of the established business. This seems strange in view of the fact that it is much more difficult to determine the actual cost of establishing the business than it is to determine the actual cost of physical property when such cost is taken as the first cost of the units now in place. A reason for turning to the actual cost method to determine the cost of the established business is found in the fact that it is considered that this allowance should cover only uncompensated losses, or the amount by which early failure to earn a fair return has not been offset by subsequent earnings in excess of a fair return. If this principle is accepted it is clear that a hypothetical reproduction process could scarcely be applied.

In a few recent cases the Wisconsin commission has considered an estimate of the cost of reproducing a paying business in fixing fair value. The reproduction method as thus used is not the comparative plant method, but an estimate of the losses that would be incurred assuming that the enterprise were to be started under present conditions. It only includes failure to earn a fair return up to the time when it is estimated that the business will have been placed on a paying basis. The estimate under this method is naturally much less than would ordinarily be found under the comparative plant method, and is ordinarily also less than the probable actual cost to the company of developing its business.

Franchise Value

The actual necessary cost of obtaining a franchise should, of course, be included in a valuation for rate purposes. Other than this the weight of practice and authority is distinctly against the

inclusion of an allowance for franchise value in a valuation for rate purposes. This position seems to be economically sound. There are two distinct functions of the franchise: One is to guarantee the integrity of the investment and the other is to make it possible for the investor to secure a reasonable reward for his enterprise in establishing the plant or railroad. The integrity of the investment is scrupulously recognized and provided for if in a valuation for rate purposes the tangible property is recognized as being rightfully in the streets or public places, and each part is valued with reference to its use in the existing operating system and not simply at its value as scrap. The function of the franchise in insuring to the investor the opportunity to secure if possible a reasonable reward for his enterprise and risk in establishing the public utility is recognized and provided for in a rate case if a rate of return on actual investment is allowed commensurate with the risk assumed. If the rate of return is fair and is based on the entire actual investment nothing further can in reason be expected.

A great deal of confusion has arisen in the consideration of this subject owing to a failure to see the fundamental distinction between valuation for rate making and valuation for public purchase. It is recognized that in a condemnation case the value of the franchise must be included. From this it is argued that unless the franchise is included also in the valuation for rate making the value of the franchise is in effect confiscated. If it is wrong and illegal to confiscate the value of the franchise in a condemnation case it is just as wrong and presumably just as illegal to confiscate such value indirectly through the rate making process. Deprivation of compensation for the use of property is no less confiscation than the actual taking of the property. The fallacy arises in a failure to realize that though in a condemnation case the valuation is the all important factor, in the determination of reasonable rates the essential thing is the total net income; and that this net income is not measured by the valuation alone but by the product of the valuation and the rate of return. If the capitalized value of the total net income allowed in a rate case is the same as the valuation for purchase purposes, due consideration will have been given to the franchise in both cases, even though in the valuation for purchase there has been a specific allowance for the franchise and in the valuation for rate purposes there has been no such allowance.

In a rate case due consideration is given to the franchise rights in the determination of the fair rate of return. The fact that the rate of return is fixed on the basis of a return adequate to induce investment in a new enterprise, although now that the enterprise in question has been successfully established persons will invest on a lower return basis, is a substantial recognition of the rights that it is the function of the franchise to protect. The franchise having thus been allowed for in the rate of return, it would be duplication to allow for it again in the valuation on which the rates are based.